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Report to the Secretary of Defense

August 2000

DEFENSE INVENTORY

Actions Needed to Evaluate Supply Purchase Options for Facilities Maintenance



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Contents

Letter		3
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Appendixes	Appendix I: Comments From the Department of Defense	24
	Appendix II: GAO Contacts and Staff Acknowledgments	26

Tables	Table 1: Installation Use of Prime Vendor Program	11
	Table 2: Military Services' Program Monitoring Efforts	15

Figures	Figure 1: Ten Geographic Regions Served by DLA's Maintenance, Repair, and Operations Prime Vendor Program	8
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Abbreviations

DLA	Defense Logistics Agency
DOD	Department of Defense



United States General Accounting Office
Washington, D.C. 20548

National Security and
International Affairs Division

B-285571

August 23, 2000

The Honorable William S. Cohen
The Secretary of Defense

Dear Mr. Secretary:

Since 1990, we have identified Department of Defense (DOD) inventory management as a high-risk area because levels of inventory were too high and management systems and procedures were ineffective.¹ We reported that adopting best business practices in inventory management and improving the reliability of financial management information are key steps toward solving these problems. Congress has also taken actions to encourage the Department to adopt best commercial practices to improve inventory management. Specifically, the National Defense Authorization Acts for Fiscal Years 1998 and 1999 required the Director of the Defense Logistics Agency and the secretary of each military department to submit schedules for implementing best commercial practices for the acquisition and distribution of selected inventory items.

For several years, DOD has been working to adopt best practices to improve the efficiency and effectiveness of its operations and its ability to respond to the war fighter's requirements. In 1997 and again in 1999, the Defense Reform Initiative report² highlighted the Defense Logistics Agency's maintenance, repair, and operations prime vendor program as one of the Department's success stories in adopting commercial best practices. Under the program, the Agency has contracted with prime vendors to provide facility maintenance supplies directly to military installations, as an alternative to using the traditional Defense supply system or direct purchases.

¹ In 1990, we began a special effort to review and report on the federal program areas that we identified as high risk because of vulnerabilities to waste, fraud, abuse, and mismanagement. This effort, which was supported by the Senate Committee on Government Affairs and the House Committee on Government Reform, brought a much-needed focus to problems that were costing the government billions of dollars.

² The Defense Reform Initiative was established in November 1997 to increase funding for weapon system modernization programs by reducing infrastructure costs and streamlining business processes.

This report assesses the Department's efforts to implement the maintenance, repair, and operations prime vendor program. Specifically, we determined (1) how much the program is being used and how selected installations are using the program and (2) whether DOD has a mechanism for evaluating the program's effectiveness relative to other procurement alternatives and for identifying and addressing implementation obstacles. We examined the implementation of the prime vendor program at 11 military installations, and although the results of this analysis cannot be extrapolated to the entire program, they provide first-hand accounts that illustrate the actual impact of the program and highlight accomplishments and opportunities for improvement.

Results in Brief

The Department of Defense has begun implementing the Defense Logistics Agency's maintenance, repair, and operations prime vendor program, but in fiscal year 1999, it covered only a small portion of business operations. The Agency has awarded prime vendor contracts to support military installations nationwide and at some overseas locations, and over 100 customers placed orders with these vendors in fiscal year 1999. These orders represented about \$59 million, or less than 10 percent of the estimated \$670 million the Department spent on facility maintenance supplies during that year. Use of the program varied widely among the installations. At 7 of the 11 installations we examined, base personnel ordered, on average, about 55 percent of facilities maintenance supplies from the prime vendor during fiscal year 1999. Of the other four installations, three did not use the program in fiscal year 1999 and one could not quantify the extent to which the prime vendor was used.

DOD does not have a mechanism to evaluate the extent to which the prime vendor program has been used to streamline logistics operations or increase overall logistics system effectiveness. In addition, DOD has not determined how the program should be used in conjunction with the other procurement methods to provide installations with the most efficient and effective supply system. Furthermore, the Defense Logistics Agency and the military departments have encountered significant issues while implementing the program that should be addressed for the program to operate as intended. For example, at some installations, ineffective working relationships among the Agency, the prime vendors, and the installations have limited the program's use. Another issue raised by installation officials was that the prime vendors' prices for facilities maintenance supplies were often higher than the price the installation would pay if the items were purchased directly from a local merchant.

We are recommending that the Secretary of Defense develop an approach to obtain the information that is needed to evaluate the use and effectiveness of the prime vendor program and identify and address implementation obstacles. The Department agreed with the contents of this report and its recommendations.

Background

DOD uses a variety of inventory items such as hardware, electrical and plumbing supplies, paint, small tools, and building materials to repair buildings and facilities at military installations around the world. These materials are commonly referred to as maintenance, repair, and operations supplies or facilities maintenance supplies. In fiscal year 1999, the Defense Logistics Agency (DLA) estimated that DOD installations worldwide spent about \$670 million for facilities maintenance supplies. In recent years, DOD has implemented two initiatives, a prime vendor program and government purchase cards, that provide military installations new alternatives to obtaining facilities maintenance supplies.³

First, in 1997, following implementation of prime vendor programs to improve the management of medical and food inventories, DLA established a prime vendor program for facilities maintenance supplies. Although prime vendors can be used in different ways, the basic concept requires a prime vendor to obtain supplies from a variety of suppliers and deliver the supplies directly to the customer within hours or days after receiving an order. In August 1998, recognizing the potential benefits that could be derived from using the prime vendor program, the Deputy Secretary of Defense directed the military services to designate points of contact to oversee implementation of the program, identify sites that should thoroughly evaluate program participation, and assist DLA in implementation.⁴ The Deputy Secretary of Defense also directed DLA to work with the military departments in evaluating potential sites and developing implementation plans for target locations. In its 1999 Defense Reform Update, DOD projected that the prime vendor program would steadily expand over the next few years, with sales through the prime

³ Facilities maintenance supplies may also be obtained from the General Services Administration and the DOD Electronic Mall, and through other procurement methods.

⁴ Department of Defense Reform Initiative Directive #45 – *Prime Vendor Contracting Program for Facility Maintenance Supplies* (Aug. 24, 1998).

vendors increasing from about \$18 million in fiscal year 1998 to \$29 million in fiscal year 1999 and up to \$56 million in fiscal year 2000.

Under the second initiative, military installations obtain facilities maintenance supplies primarily from local merchants and pay for those supplies using government purchase cards⁵ for orders of \$2,500 or less. Purchase cards are currently the more commonly used method by which military installations obtain facilities maintenance supplies. For orders that exceed \$2,500 (the micropurchase threshold), installation contracting offices generally contract with suppliers to provide the required items using a competitive selection process. Supply operations at an installation can involve a few to more than 20 military and civilian personnel and require facilities, vehicles, and other resources to order, purchase, transport, store, and distribute inventory.

The National Defense Authorization Act for Fiscal Year 1998 required that at least 90 percent of DOD's purchases under the micropurchase threshold be made with the purchase card by October 1, 2000. More recently, in the 1999 Defense Reform Update, the Secretary of Defense established a goal of using purchase cards for at least 90 percent of all Defense purchases of \$2,500 or less by January 2000. DOD met its goal, reporting that over 91 percent of micropurchases in fiscal year 1999 were made with purchase cards.

Use of the Facilities Maintenance Prime Vendor Program

DLA has awarded prime vendor contracts to provide facilities maintenance supplies to military installations nationwide and at some overseas locations. As of the end of fiscal year 1999, about 40 percent of the potential customers identified by DLA had begun placing orders with the prime vendors. Overall, those customers' purchases amounted to less than 10 percent of the total estimated facilities maintenance supplies purchased throughout DOD for that year. At the 11 installations we examined, each installation used the prime vendor program to different degrees. Base personnel at seven installations that used the program in fiscal year 1999 and were able to provide us with usage data, ordered, on average, about 55 percent of facilities maintenance supplies from the prime vendor. For example, at Camp Lejeune, North Carolina, installation personnel

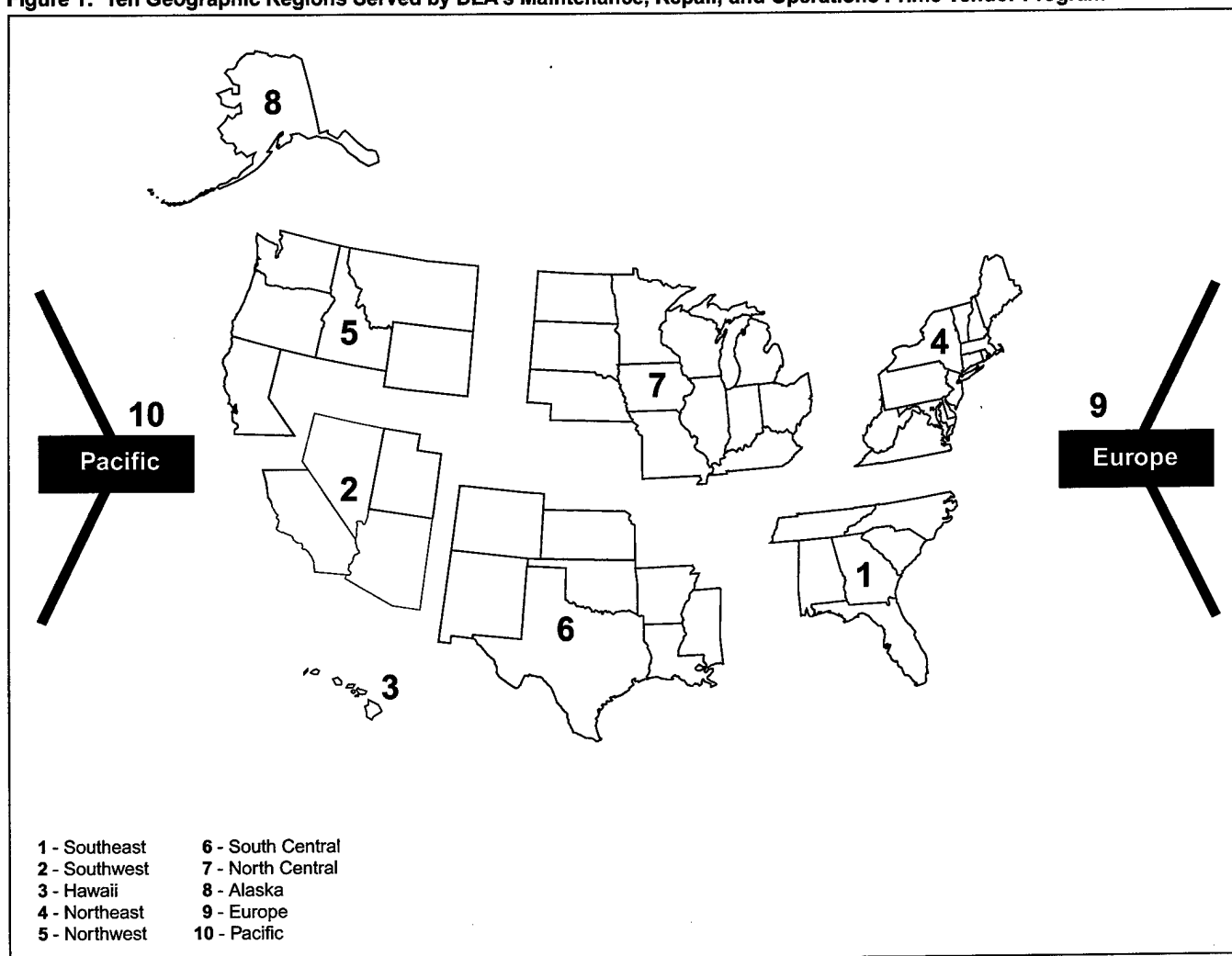
⁵ Purchase cards are commercial credit cards—either MasterCard or VISA cards—that are issued to authorized DOD military and civilian users to acquire and pay for low-cost supplies and services.

purchased about 21 percent of facilities maintenance supplies from the prime vendor, the remainder of these items were purchased from local merchants using government purchase cards or from other sources. In contrast, personnel at Parris Island Recruit Depot, South Carolina, obtained 84 percent of all facilities maintenance supplies through the prime vendor in fiscal year 1999. The differences in how each installation used the prime vendor program were attributable primarily to decisions made by installation commanders, which were based on prime vendor capabilities, local vendor support, and openness to using new business practices.

**Nationwide Contracts
Awarded for Prime Vendor
Program**

As of August 1999, DLA had awarded contracts to five prime vendors to provide facilities maintenance supplies to military installations nationwide, as well as to customers in Japan (including Okinawa) and South Korea. The 1-year contracts between DLA and the vendors include four 1-year renewal options and require the prime vendors to support military installations within 10 geographic regions. The Southeast, Southwest, Northeast, South Central, and Hawaii regions are each served by two of the five vendors, with each one supporting specific military installations within a region. The other four regions (Alaska, Northwest, North Central, and Pacific) are each supported by one vendor per region. Prime vendor contracts for installations in Europe are pending. (See fig. 1.)

Figure 1: Ten Geographic Regions Served by DLA's Maintenance, Repair, and Operations Prime Vendor Program



Source: Defense Logistics Agency.

DLA has contracted with the prime vendors to provide military customers with a single source of supply to meet all of their facilities maintenance inventory requirements. The prime vendor is required to provide an electronic ordering system, electronic catalogues that have been tailored to each customer's needs, 72-hour delivery of inventory that is in-stock, 24-hour delivery of inventory for emergency repairs, and direct delivery of inventory to multiple locations. According to DLA, using the prime vendor for these services can reduce an installation's inventory levels as well as storage, contracting, and administrative costs and provide installation personnel greater flexibility in selecting products. Both DLA and the prime vendors apply surcharges on each purchase an installation makes through the program. These surcharges are included in the price the installations pay for each item purchased. DLA applies a 3.9-percent surcharge, while the prime vendors' surcharges range from 10 to 30 percent on each item purchased.⁶

In contrast to the requirements of DLA's program, the relationship between some private sector companies and the prime vendors has been expanded to include all aspects of inventory management. For example, one private sector company we visited has completely integrated its prime vendor into day-to-day operations. Prime vendor employees are responsible for all aspects of facilities maintenance inventory management from ordering supplies, storing inventory, and delivering supplies to the customer's end users. The prime vendor also provides the customer with management reports, inventory usage information, and consolidated billing that reduces the administrative burdens on the customer. Much of the savings the company has achieved by using the prime vendor as an integrated supplier have resulted from reducing administrative costs associated with purchasing, receiving, stocking, and delivering supplies; and preparing purchase orders and processing invoices and eliminating the need for investments in inventory.

⁶ Prime vendor surcharges vary by vendor, region, installation, and commodity. Under the prime vendor contracts, each vendor has the flexibility to adjust the surcharge applied to each item, within the 10- to 30-percent range, as long as the surcharge is below the prescribed 30-percent ceiling.

Installations Use the Program to Varying Degrees

Although DLA had contracted for prime vendor services nationwide and in some overseas locations, overall, the extent to which military installations were using the prime vendors varied. As of the end of fiscal year 1999, DLA had identified 278 potential customers for the prime vendor program.⁷ Of these customers, 110 (about 40 percent) had placed at least one order with the prime vendor during fiscal year 1999. These orders amounted to about \$59 million in purchases in fiscal year 1999, which was about twice the \$29 million in sales that the Department projected for that year. Overall, the 1999 prime vendor sales represented less than 10 percent of the estimated \$670 million DOD had budgeted for facilities maintenance supplies.

Also, each installation we examined used the prime vendor program to different degrees and installation officials viewed the prime vendor as one of several alternative sources of facilities maintenance supplies. For example, at Camp Lejeune, installation personnel purchased about 21 percent of their facilities maintenance supplies from the prime vendor in fiscal year 1999. The remainder of their purchases were made through local merchants using the government purchase card (about 53 percent) or another alternative method (about 26 percent). At Fort Stewart, Georgia, installation personnel purchased about 33 percent of facilities maintenance supplies through the prime vendors, purchasing the majority of their supplies using their purchase cards. In contrast, four other installations we examined (Kadena Air Force Base, Okinawa; Port Hueneme, California; and Marine Corps installations at Barstow, California; and Parris Island, South Carolina) used the prime vendor as the source for over 50 percent of facilities maintenance supplies in fiscal year 1999. To encourage use of the prime vendor program, the commander of the Marine Corps Logistics Base in Barstow has directed that the prime vendor will be the primary source for purchasing facilities maintenance supplies and that government purchase cards will only be used for purchasing such supplies in emergency situations, when the prime vendor cannot meet compressed time constraints. Table 1 summarizes the extent to which the prime vendor has been used at the 11 installations.

⁷ This does not equate to 278 installations, as there may be more than one "customer" at an installation. For example, at the Naval Base Ventura County, Port Hueneme, California, five separate organizations participate in the prime vendor program.

Table 1: Installation Use of Prime Vendor Program

Installation	Extent to which prime vendor program is used
Air Force	
Kadena Air Force Base, Okinawa	This installation obtained about 57 percent of facilities maintenance supplies through the prime vendor in fiscal year 1999. Installation officials expect to increase reliance on the prime vendor to obtain about 95 percent of facilities maintenance supplies in fiscal year 2000.
Shaw Air Force Base, South Carolina	This installation did not use the prime vendor program in fiscal year 1999. It began using the program in October 1999 and as of May 2000 had obtained about 20 percent of facilities maintenance supplies through the prime vendor.
Army	
Fort Hood, Texas	This installation did not use the program in fiscal year 1999. It began using the program in December 1999 and as of April 2000 had obtained about 12 percent of facilities maintenance supplies from the prime vendor for this fiscal year.
Fort Jackson, South Carolina	This installation did not use the program in fiscal year 1999 or 2000. This installation piloted the prime vendor program for the Army, but it withdrew from the program in April 1998, after 12 months, because of concerns about item prices and customer service. DLA offered Fort Jackson the opportunity to rejoin the program with a different prime vendor, but installation officials declined to participate. Instead, in November 1999, Fort Jackson established its own prime vendor contracts with four local vendors covering about 400 items.
Fort McCoy, Wisconsin	This installation obtained about 31 percent of all facilities maintenance supplies through the prime vendor (primarily for large dollar value items over \$2,500) during fiscal year 1999, and increased usage to 57 percent as of April 2000.
Fort Stewart, Georgia	This installation obtained about 33 percent of all facilities maintenance supplies through the prime vendor in fiscal year 1999; officials expect to expand use of the program this year.
Marine Corps	
Camp Lejeune, North Carolina	This installation obtained about 21 percent of all facilities maintenance supplies through the prime vendor in fiscal year 1999 (primarily for large dollar value items over \$2,500). It recently switched to another prime vendor, and officials expect to increase usage for fiscal year 2000.
Logistics Base, Barstow, California	This base obtained about 63 percent of all facilities maintenance supplies through the prime vendor in fiscal year 1999.
Recruit Depot, Parris Island, South Carolina	The depot obtained about 84 percent of all facilities maintenance supplies through the prime vendor in fiscal year 1999.
Air Ground Combat Center, Twentynine Palms, California	Installation officials were unable to quantify the extent to which the prime vendor program was used in fiscal years 1999 and 2000. This installation joined the program in May 1998 and switched to a new prime vendor in June 1999.
Navy	
Naval Base Ventura County, Port Hueneme, California	This base obtained 100 percent of supplies needed for construction projects that require that the materials be accumulated and stored off-site for just-in-time delivery to the construction site through the prime vendor in fiscal year 1999.

Source: GAO's analysis of installation information.

At most of the installations we visited, officials stated that they believed that the prime vendor program had not resulted in significant cost reductions associated with reducing inventory, personnel, or infrastructure. When inventory and personnel reductions occurred, the reductions were the result of reengineering business processes and DOD-wide downsizing efforts and, for the most part, the reductions took place before the installations joined the prime vendor program. Installation officials were unable to quantify the extent to which these reductions have occurred because historical records were not retained. Some installation officials stated that using the program had enabled them to more easily cope with previous personnel reductions but had not resulted in additional downsizing of base supply staff.

Factors that Influence Implementation Decisions at the Installations

Several factors play a significant role in determining the extent to which each installation uses the prime vendor program. The military services have delegated to each installation commander the authority to decide whether the installation will order supplies from the prime vendor and the role the prime vendor will play at that installation. The services also encourage, or in some cases discourage, the installations' participation in the program. For example, the Marine Corps, in an October 1998 memorandum, "strongly encouraged" installation commanders to take advantage of the program. The Army's Training and Doctrine Command, however, issued a memorandum in April 1998 that terminated Fort Jackson's participation in the program and stated that such a program is not "a cost-effective method for this command in today's environment."⁸

Officials from each military department stated that they believe the installation commanders are in the best position to make these determinations and should be allowed maximum flexibility in determining the methods their installations use to obtain facilities maintenance supplies. Several factors, such as (1) the prime vendor's capabilities, (2) the availability of local supply sources, and (3) the willingness of installation personnel to accept and use this new business practice, influences installation decisions on how much the prime vendor program is used.

One factor that influences the degree to which the program is used by individual installations is the prime vendor's capabilities. Officials at

⁸ DLA officials have reviewed the prime vendor's performance at Fort Jackson and disagree with the Training and Doctrine Command's assessment.

several of the installations we visited told us that they would like the prime vendor to manage their facilities maintenance inventory. Some prime vendors have extensive experience in integrated supplier relationships and are well equipped to purchase, store, and distribute facilities maintenance supplies for their military customers. Other prime vendors do not have the facilities or the experience to perform such functions. In the past year, DLA has allowed installations to switch prime vendors to improve customer satisfaction by allowing installations to work with prime vendors that can better meet the installations' needs. For example, the Marine Corps Air Ground Combat Center at Twentynine Palms switched to a new prime vendor in June 1999, after about a year in the program, because the first vendor was repeatedly unable to meet delivery dates and did not provide the level of customer service expected. DLA recently allowed two more Marine Corps installations to switch prime vendors for similar reasons.

A second factor that influences the extent to which the prime vendor is used is an installation's geographic location. Of 11 installations we examined, those located in overseas or remote areas—such as Kadena Air Force Base and the Marine Corps Recruit Depot at Parris Island—were likely to use the prime vendor more extensively than those in larger areas. Installations in larger, metropolitan areas—such as Shaw Air Force Base, located near Columbia, South Carolina, and Fort Stewart, located near Savannah, Georgia—were more likely to rely on local merchants to obtain facilities maintenance supplies. Installations located in metropolitan areas generally had more options in the surrounding area, including local merchants and national chains, from which to obtain facilities maintenance supplies.

A third factor that influences how much the program is used is the willingness of supply personnel at each location to accept and use new business practices. To ease the transition to a prime vendor program, officials at one private sector firm we contacted told us that they implemented their own facilities maintenance prime vendor program on a unit-by-unit basis and that joining the program was always voluntary. The officials also emphasized that educating end users about the program before beginning implementation is critical to success. In addition, these officials commented that the program must be tailored to meet the specific needs of the customer and that customer feedback must be continuously encouraged and promptly addressed.

Program Results Not Being Evaluated, and Implementation Issues Remain

DOD does not monitor the extent to which the program is being used to streamline logistics operations or measure the program's impact on the overall supply system. Neither DOD nor the military departments are collecting the information necessary to evaluate the program's effectiveness or to determine how the prime vendor should be used in conjunction with the purchase card or other procurement methods to provide the installations with the most efficient and effective supply system. Further, DLA and the military departments have encountered several issues while implementing the prime vendor program that should be addressed for the program to operate as intended.

Management Information Needed to Assess Prime Vendor Program

Management information that would enable DOD to evaluate the prime vendor program's effectiveness and determine how the program should be used in conjunction with other programs is not available. Specifically, DOD has not collected the information needed to evaluate and compare the estimated costs and benefits of using the program to other procurement methods—primarily the government purchase cards. While DLA performs some limited monitoring of usage of the prime vendor program, it is not sufficient to measure actual savings realized from using the program at the installation level. For example, DLA officials monitor the number of installations using the program and the volume of prime vendor sales made to each installation. They also monitor various customer service aspects of the program, such as orders filled and on-time delivery, to provide a basis for future contracting decisions. However, DLA does not collect, on a broad scale, information on the costs associated with operating the program at the installations or the savings, if any, associated with using the prime vendor program (such as inventory or infrastructure reductions) rather than using other procurement methods to obtain facilities maintenance supplies. Likewise, the military departments have not developed mechanisms to capture and evaluate the costs and benefits of participating in the program. As shown in table 2, efforts to monitor the prime vendor program vary by military department.

Table 2: Military Services' Program Monitoring Efforts

Military service	Monitoring efforts
Air Force	Collects program data (such as items purchased, item prices, length of time required to obtain a quote from the vendor, and delivery dates) from its Civil Engineering Material Acquisition System to monitor Air Force installations' use of the facilities maintenance prime vendor program.
Army	Formed a working group to collect program data similar to that collected by DLA (i.e., installations using the program and sales volume); the working group also shares its data with DLA program officials.
Marine Corps	Relies heavily on DLA program data and monitors installation satisfaction through regular contact with installation personnel and program review sessions with installations, DLA, and prime vendors.
Navy	Does not actively monitor installation participation in the program.

Source: GAO's analysis.

In addition to limited information on the cost and effectiveness of the prime vendor program, DOD does not have complete information on the estimated cost of operations using the purchase card program. Our work on DOD's purchase card program has shown that actual savings estimates associated with the program are unavailable.⁹ The Army Audit Agency has estimated savings of \$92 per transaction when supplies or services are purchased using government purchase cards compared to using the traditional procurement methods. However, comparable data for other DOD components are not available. In its *Annual Performance Report for Fiscal Year 2000*, DOD reports that using the purchase card has resulted in sizable manpower-related savings but does not provide specific savings estimates.

Program Implementation Issues Can Hinder Progress

DLA and the military departments have encountered several obstacles while implementing the prime vendor program that provide lessons learned for future implementation. For example, in some cases, DLA, the vendors, and the customers did not work together effectively to implement the program. Other implementation obstacles, such as high item prices and information technology, have frustrated program participants and may have deterred potential customers from using the program. DOD plans to use its Logistics Reform Senior Steering Group as a forum to address such implementation obstacles.

⁹ *Defense Management: Electronic Commerce Implementation Strategy Can Be Improved* (GAO/NSIAD-00-108, July 18, 2000).

Working Relationship Issues

The working relationship among installation personnel, DLA officials, and prime vendor representatives is a critical factor directly related to the program's success at any given installation. As discussed earlier, once DLA awards the prime vendor contracts, installation commanders determine the extent to which each installation will use the initiative in its operations. The willingness of DLA and the prime vendor to respond to installation personnel's concerns, personalities, and even cultural differences may affect program effectiveness at a particular installation. Overall, at the installations we visited such relationships have been fairly productive. However, when this is not the case, it has led to the program failing at that particular installation. All three parties must work together to make the program successful.

At installations we visited where the relationship was one of cooperation and partnership, the program had flourished. For example, at the Marine Corps Logistics Base at Barstow, DLA, prime vendor, and installation personnel have developed a cooperative working relationship and the program has been successful. As discussed earlier in this report, the base commander has directed that the prime vendor will be the primary source for purchasing facilities maintenance supplies.

Without such cooperation, the program is likely to fall short of expectations. For example, officials at Fort Jackson, one of the pilot test sites, stated that they did not believe DLA and the prime vendor were responsive enough to their concerns regarding slow delivery times, the lack of a useful electronic catalog, and other prime vendor performance issues. The officials also noted that they believed that DLA representatives took their complaints as attempts to undermine the program. As a result, during the 12-month pilot period, these problems were never satisfactorily resolved, leading to the installation's withdrawal from the program.

Item Pricing Issues

At most of the installations we visited, officials expressed concerns that the prime vendors' prices for facilities maintenance supplies were too high. The prime vendors price for individual facilities maintenance items, with added vendor and DLA surcharges, can be higher than the price the installation would pay if it purchased the same items directly from a local merchant. For the installations we visited, we found that the prime vendor often purchased facilities maintenance supplies for a particular installation from the same local merchants the installation used prior to joining the program. This was due, in part, to the installation personnel's requests that the vendor obtain the specific brand or type of items they had used in the past from the same local merchants. Installation supply personnel have

stated they are reluctant to sever long-standing relationships with local merchants and encourage prime vendors to continue patronizing local businesses. Such emphasis on purchasing supplies from local merchants tends to preclude the prime vendors from leveraging their buying power and using economies of scale to obtain the most favorable price from larger, national businesses.

DLA has not performed a nationwide pricing review to determine whether the prime vendors' prices are typically higher, lower, or about the same as the prices charged by local merchants; however, it has reviewed prices at some individual installations. The reviews have determined that on many items the prime vendor's price is lower than the local price available. For example, at one location, DLA reviewed the prices of 40 selected items and found that the prime vendor's price was lower than the local merchant's price on over 30 of the items. However, according to the DLA program manager, when reviewing the results of the comparison, supply personnel tended to focus on the six or seven items that were more expensive when purchased from the prime vendor.

According to DLA officials, concern over item price increases is a major obstacle when a prime vendor program is first introduced to potential military customers. DLA officials admit that the program may increase the unit price of some items. However, they noted that this increase should be offset by (1) a larger, but less visible, reduction in total DOD costs due to lower administrative, overhead, and infrastructure expenses; (2) better product quality; and (3) improved customer service due to greater availability of parts and faster deliveries to the customer. A comprehensive evaluation of unit price increases that would consider these total system costs, product quality, and customer service is characterized as a "best value" analysis.

Getting the customer to shift from a unit price to a best value focus is difficult. One DLA approach has been to conduct baseline cost comparisons at specific implementation sites to show the customer how the total cost under the new program is lower than the total cost under the traditional supply system. However, it may be difficult, if not impossible, to develop similar baseline comparisons on a broader scale because of significant weaknesses in the reliability of reported DOD inventory data and cost information. Consequently, the Department uses obligation data

or other estimates of actual cost.¹⁰ According to DLA officials, many installations are reluctant to participate in baseline analyses.

Information Technology Issues

Another obstacle affecting program implementation centers on the difficulty installations face when ordering items from the prime vendors. DLA's contracts with the prime vendors require that the vendors provide an electronic ordering system. However, at several of the installations we visited, electronic ordering capability is not yet available because the prime vendor has not yet developed an electronic catalog of frequently used items for that particular installation. As a result, installation personnel must place orders with the prime vendor via telephone or fax machine. At other installations, the prime vendor has provided electronic ordering capability using the Internet. However, according to installation personnel, placing orders with the prime vendor via the Internet can be a slow and tedious process, sometimes taking hours to complete one order, due to security firewalls and access restrictions.

In addition, incompatibility between DOD's and the vendor's information systems sometimes presents problems, requiring installation personnel to record each order twice—once in the prime vendor's system and once in the service's system. For example, in early 1998, Shaw Air Force Base was the first Air Force installation to participate in a test of the prime vendor program. During the test, incompatibility between the vendor's information system and the Air Force's Civil Engineering Material Acquisition System¹¹ required each order to be entered twice—once to order from the vendor and the second time to input the order information into the Air Force system. The Air Force customers deemed this process too time-consuming and chose to delay participation in the program until an interface with the prime vendor's system could be developed. After a yearlong test of the interface, Air Force installations began joining the program in September 1999. To date, DLA and the Air Force have developed an information system link with three of the four prime vendors. DLA has also worked with the Army to create an interface between the Army's Supply 2000 system¹² and the Defense Supply Center in Philadelphia, Pennsylvania,

¹⁰ *Department of Defense: Progress in Financial Management Reform* (GAO/T-AIMD/NSIAD-00-163, May 9, 2000).

¹¹ This system is an Air Force legacy system that installations use to track inventory usage and account for expenditures by building number.

¹² Supply 2000 is a software application supporting facility maintenance activities.

which manages the prime vendor program. This interface eliminates the need for dual transaction entry and should be available to all Army installations by the end of this fiscal year. The Navy, the Marine Corps and DLA, however, have not yet developed solutions to this problem.

Logistics Reform Senior Steering Group Provides a Forum to Address Implementation Obstacles

In response to our January 2000 report on DLA's best practice initiatives, DOD stated that it will use its Logistics Reform Senior Steering Group, which is comprised of senior-level logistics officials from each military department, as a forum to address obstacles to implementing DLA's best practice initiatives.¹³ According to DOD, this group will promote participation by DOD activities in those initiatives to the extent they provide the combination of quality, timeliness, and cost that best meet DOD's requirements. This group will also highlight the benefits of participating in the initiatives, consider appropriate outcome measures, and share lessons learned. DOD further stated that DLA would take the lead in presenting these issues to the group.

Conclusions

While DOD has developed initiatives to improve the acquisition of facilities maintenance supplies, it has not collected information that is needed to determine if the prime vendor, the purchase card, or some combination of these and other methods would provide DOD with the most cost-effective and efficient way of buying facilities maintenance supplies. Nor is the Department collecting information on implementation issues such as relationships among the Defense Logistics Agency, vendors, and military installations; concerns over unit price; and information technology issues. Further, the Department's continuing problems in developing reliable cost information limit broad scale cost comparisons. If DOD is to continue implementing the prime vendor program, it must have information on the costs associated with operating the program and the savings associated with using the prime vendor at the installation. Without this information, it is uncertain what procurement method should be pursued, opportunities to reduce logistics costs and improve customer service may be lost, and the program may not operate in its most efficient and effective manner.

¹³ *Defense Inventory: Opportunities Exist to Expand the Use of Defense Logistics Agency Best Practices* (GAO/NSIAD-00-30, Jan. 26, 2000).

Recommendations

To assist military installations in choosing the most efficient and effective methods of obtaining facilities maintenance supplies, we recommend that the Secretary of Defense direct the Director, Defense Logistics Agency, and the secretary of each military department to undertake a cooperative effort to determine how the prime vendor program best fits within DOD's operations in conjunction with other procurement methods, particularly the government purchase card. This effort should include

- developing a mechanism to monitor and measure the cost and benefits of using the facilities maintenance prime vendor program when compared to other procurement methods and to identify implementation obstacles as they are encountered at each military installation and
- establishing an analysis model that considers the estimated total cost, product quality, and customer satisfaction and that installation commanders can use to determine the appropriate mix of prime vendor, purchase card, and other procurement methods for procuring facilities maintenance supplies at each installation.

Agency Comments

DOD agreed with our recommendation and stated that the Defense Logistics Agency will take the lead in working with the military departments to develop a mechanism to monitor the costs and benefits of using the facilities maintenance prime vendor program and identify implementation obstacles. DOD further stated that the Defense Logistics Agency will also take the lead in working with the military departments to develop an analysis model that installation commanders can use to determine the appropriate degree to which to use the program. DOD expects completion of these efforts by March 2001. DOD's comments are reprinted in their entirety as appendix I.

Scope and Methodology

To determine the extent to which the prime vendor program was being used, we met with officials from DLA headquarters, Washington, D.C., and DLA's prime vendor program manager located at the Defense Supply Center, Philadelphia, Pennsylvania. In addition, we analyzed information on the overall status of program implementation in terms of (1) contracts awarded to prime vendors, (2) potential customers identified by DLA and number of installations participating, and (3) total prime vendor program sales data for fiscal year 1999.

To determine how the program was being implemented at selected installations and identify opportunities for improving program implementation, we visited or obtained information from 11 installations. To select the installations, we asked DLA officials to identify locations where the program was being used and provide information on the volume of purchases made through the prime vendors. From information provided by the officials, we judgmentally selected 11 installations to visit or obtain information from. To ensure that we obtained a variety of views, we selected installations representing each military service and served by each of the five prime vendors, as well as installations that are frequent users of the program and installations that do not use the program as much. We visited Fort Hood, Texas; Fort Jackson, South Carolina; Fort Stewart, Georgia; Shaw Air Force Base, South Carolina; Parris Island Marine Corps Recruit Depot, South Carolina; Marine Corps Logistics Base, Barstow, California; Marine Corps Air and Ground Combat Center, Twentynine Palms, California; Camp Lejeune Marine Corps Base, North Carolina; and Naval Base Ventura County, Port Hueneme, California. At each installation, we met with logistics personnel and end users involved with the prime vendor program to obtain information on implementation experiences, customer satisfaction, and lessons learned from implementing the program at their installation. We also contacted officials at Fort McCoy, Wisconsin, and Kadena Air Force Base, Okinawa, by telephone and electronic mail to obtain their views on implementing the program and lessons learned.

To obtain the prime vendors' perspective on the program and discuss implementation experiences and lessons learned, we met with representatives of Cameron and Barkley at its Charleston, South Carolina, facility and Graybar Incorporated at its Dallas, Texas, facility. We selected Cameron and Barkley because it was located near several of the military installations we visited. We selected Graybar Incorporated because it also supplied one of the private sector companies we contacted.

To provide a private sector perspective on best practices for managing facilities maintenance inventory, we visited or contacted several private sector companies who had adopted leading-edge business practices to manage facilities maintenance inventories. Specifically, we visited Texas Instruments in Dallas, Texas, to obtain information on its long-standing facilities maintenance prime vendor program. While at Texas Instruments, we met with company officials, as well as Graybar representatives, to discuss their experiences and lessons learned from implementing a facilities maintenance prime vendor program. We also obtained similar

information from officials of Coors Brewing Company, in Elkton, Virginia, and the Saturn Corporation, in Springhill, Tennessee.

We conducted our review from October 1999 through June 2000 in accordance with generally accepted government auditing standards.

This report contains recommendations to you. The head of a federal agency is required under 31 U.S.C. 720 to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Reform not later than 60 days after the date of the report and to the Senate and House Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of this report.

We are sending copies of this report to the appropriate congressional committees. We are also sending copies to Lieutenant General Henry T. Glisson, Director, Defense Logistics Agency; the Honorable Louis Caldera, Secretary of the Army; the Honorable Richard Danzig, Secretary of the Navy; the Honorable F. Whitten Peters, Secretary of the Air Force; General James L. Jones, Commandant of the Marine Corps; and the Honorable Jacob Lew, Director, Office of Management and Budget. We will make copies available to others upon request.

If you or your staff have any questions concerning this report or wish to discuss the matter further, please contact me at (202) 512-8412. Key contributors to this report are acknowledged in appendix II.

Sincerely yours,



David R. Warren, Director
Defense Management Issues

Comments From the Department of Defense



OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON
WASHINGTON DC 20301-3000

AUG 3 2000


Mr. David R. Warren
Director, Defense Management Issues
National Security and International
Affairs Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Warren:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) draft report, "DEFENSE INVENTORY: Actions Needed to Evaluate Supply Purchase Options for Facilities Maintenance," June 26, 2000 (GAO Code 709442/OSD Case 2044). The DoD generally concurs with the draft report. The DoD agrees that prime vendor capabilities and the geographic location of an installation are crucial factors that influence the degree to which the facilities maintenance prime vendor program is used. The DoD also agrees with the private sector firm cited in the draft report that a facilities maintenance prime vendor program should be implemented on a voluntary, unit-by-unit basis, with a program tailored to meet the specific needs of the customer and ongoing customer feedback that is promptly addressed.

Detailed comments on the draft report recommendation are included in the enclosure. The DoD appreciates the opportunity to comment on the draft report.

Sincerely,


for Roger W. Kallock
Deputy Under Secretary
of Defense (Logistics)

Enclosure



GAO DRAFT REPORT - DATED JUNE 26, 2000
GAO CODE 709442/OSD CASE 2044

**"DEFENSE INVENTORY: ACTIONS NEEDED TO EVALUATE SUPPLY PURCHASE
OPTIONS FOR FACILITIES MAINTENANCE"**

**DEPARTMENT OF DEFENSE COMMENTS TO
THE GAO RECOMMENDATION**

RECOMMENDATION: The GAO recommended that the Secretary of Defense direct the Director, Defense Logistics Agency and the Secretary of each Military Department to undertake a cooperative effort to determine how the prime vendor program best fits within DoD's operations in conjunction with other procurement methods, particularly the government purchase card. This effort should include:

- Developing a mechanism to monitor and measure the cost and benefits of using the facilities maintenance prime vendor program when compared to other procurement methods and to identify implementation obstacles as they are encountered at each military installation; and
- Establishing an analysis model that installation commanders can use to determine the appropriate mix of prime vendor, purchase card, and other procurement methods for procuring facilities maintenance supplies at each installation taking into consideration the estimated total cost, product quality and customer satisfaction.

DoD RESPONSE: Concur. The Defense Logistics Agency will take the lead in working with the Military Departments to develop a mechanism to monitor the costs and benefits of using the maintenance prime vendor program and identify implementation obstacles. The Defense Logistics Agency will also take the lead in working with the Military Departments to develop an analysis model that installation commanders can use to determine the appropriate degree of use of the prime vendor program. Estimated completion date is March 2001.

GAO Contacts and Staff Acknowledgments

GAO Contacts

Charles Patton (202) 512-4412
Robert Repasky (202) 512-9868

Acknowledgments

In addition to those named above, Penney Harwell, Robert Malpass, and Adam Vodraska made key contributions to this report.

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